

Letter of Findings: 01-20130366
Individual Income Tax
For the Years 2009, 2010, and 2011

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 require the publication of this document in the Indiana Register. This document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective as of its date of publication and remains in effect until the date it is superseded by the publication of another document in the Indiana Register.

ISSUE

I. Individual Income Tax – Imposition – Burden of Proof.

Authority: IC § 6-8.1-5-1; IC § 6-8.1-5-4; Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Indiana Dep't. of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); [45 IAC 3.1-1-66](#).

Taxpayer protests the assessment of additional individual income tax.

STATEMENT OF FACTS

Taxpayer is a shareholder of an Indiana S corporation ("Corporation"), which operates a convenience store/gas station in Indiana. In late 2012, the Indiana Department of Revenue ("Department") audited the Corporation's business records. Pursuant to the audit, the Department found that the Corporation failed to maintain adequate records as statutorily required. Based on the best information available at the time of the audit, the Department thus determined that the Corporation had additional taxable sales, which resulted in additional income of the Corporation. The Corporation's income flowed through to its shareholder, Taxpayer, as a result. The Department's audit assessed the Corporation's additional sales tax. In a separate audit investigation, the Department assessed Taxpayer additional income tax.

Taxpayer protested the assessment of tax. A phone hearing was held. This Letter of Findings ensues and addresses Taxpayer's protest of individual income tax assessment. Please refer to Letter of Findings 04-20130355 (March 2014), which addresses the S corporation's protest of sales tax assessment. Additional facts will be provided as necessary.

I. Individual Income Tax – Imposition – Burden of Proof.

DISCUSSION

The Department's sales/use tax audit led to an investigation of Taxpayer's income tax filings. The Department found that the Corporation failed to maintain its source documents, including cash register tapes (also known as z tapes) and determined that the Corporation had additional income from sales inside the store, resulting in additional income tax against Shareholder. Taxpayer, to the contrary, claimed that the Department's assessment is incorrect. Specifically, Taxpayer disagreed with the Department's audit methodology, claiming that the Department's audit did not consider some of Corporation's purchases were exempt, which would have reduced its tax liability.

As a threshold issue, all tax assessments are prima facie evidence that the Department's claim for the unpaid tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007); Indiana Dep't. of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012).

IC § 6-8.1-5-1(b), in relevant part, states "[i]f the department reasonably believes that a person has not reported the proper amount of tax due, **the department shall** make a proposed assessment of the amount of the unpaid tax **on the basis of the best information available to the department**. The amount of the assessment is considered a tax payment not made by the due date and is subject to [IC 6-8.1-10](#) concerning the imposition of penalties and interest." (**Emphasis added**).

IC § 6-8.1-5-4(a) further provides:

Every person subject to a listed tax must keep books and records so that the department can determine the amount, if any, of the person's liability for that tax by reviewing those books and records. **The records referred to in this subsection include all source documents necessary to determine the tax, including invoices, register tapes, receipts, and canceled checks.** (**Emphasis added**).

During the audit period, both the Corporation and Taxpayer failed to maintain and produce adequate records despite of the Department's field auditor's repeated requests. The Department's audit noted that, in relevant part, that:

Taxpayer did not present for audit source sales documents (cash register tapes /z-tapes). From the early stages of the audit, the auditor instructed POA to advise Taxpayer to retain all z-tapes so Taxpayer could provide source documents for audit. Because notification of the audit was in late 2012, the reporting year 2012 was included in the audit period and as such Taxpayer had sufficient notification to retain source documents for October through December 2012. Additionally, POA was also advised to instruct Taxpayer to

retain all future z-tapes as some early month 2013 z-tapes may be . . . relied upon to lend support to reported or audited sales.

Ultimately, Taxpayer did not retain or provide any z-tapes during the audit even when the auditor on March 1, 2013, requested the February 2013 Close Report (z-tape). Taxpayer stated [that] it was not available.

As an alternative, the Department eventually reviewed records of the Corporation's purchases and bank accounts although both records were incomplete. Based on the best information available at the time of the audit, the Department proceeded to conclude the audit. The audit determined that the Corporation had additional taxable sales, which resulted in additional corporate income, which in turn flowed through to Taxpayer pursuant to [45 IAC 3.1-1-66](#).

Taxpayer asserted that the audit's "methodology is incorrect because it does not match the verifiable bank records, because it does not match the original spreadsheet records of [Corporation], and because it does not match the actual purchase invoices of [Corporation]." Taxpayer also asserted that the audit did not "include Stanz Cheese and Gordon's Food Services in its exemption percentage calculation," which could have reduced Taxpayer's tax liability. To support its protest, Taxpayer's representative compiled several Excel Spreadsheets, which contained Taxpayer's numbers as compared to the Department's audit workpapers. However, without the required source documentation to support Taxpayer's numbers, the representative's Excel Spreadsheets could not be verified. In addition to copies of its 2009, 2010, 2011, and 2012 monthly bank statements, Taxpayer submitted a copy of its "Sales Report[s]," which was information compiled by Taxpayer and manually recorded in an Excel worksheet created by Taxpayer. Relying on its "Sales Reports" as its source documents, Taxpayer claimed the Department's audit assessments were incorrect.

Taxpayer is mistaken. First, pursuant to IC § 6-8.1-5-4(a), Taxpayer and Corporation are required to keep books and records, which are "all source documents . . . including invoices, register tapes, receipts, and canceled checks" so the Department can determine Taxpayer's liability. Taxpayer and Corporation did not do so. Rather, Taxpayer claimed that Corporation's bank statements and "Sales Reports" are his source documents. Upon review, however, the Department is not able to agree. The bank statements simply summarized its monthly financial transactions, such as deposits, transfers, or withdrawals for the years at issue, concerning its two bank accounts. The bank statements failed to show any sales transactions occurred inside Corporation's convenience store during the tax years at issue and the amount of the sales collected for each transaction. Thus, the Department is not able to agree with Taxpayer that its bank statements are the source documentation under IC § 6-8.1-5-4(a).

Additionally, Taxpayer's "Sales Reports" were manually compiled by Taxpayer on a daily and/or monthly basis. Taxpayer's "Sales Reports" contained the total sales tax amount in each of eight categories: "FOUNTAIN," "DELI TAX," "POP," "CANDY," "GROTAX," "CAT15," "CIGARETTE," and "MERCHANDISE." Taxpayer then totaled the sales tax for that month for each of those categories. Taxpayer's "Sales Reports" did not contain any records of each retail transaction (i.e., items sold per sale) occurred inside the store; rather, the "Sales Reports" summarized Corporation's total sales of each category for specific day or month. Thus, the Department also is not able to agree with Taxpayer that the "Sales Reports" are the source documentation under IC § 6-8.1-5-4(a).

Taxpayer and Corporation not only failed to adequately maintain the statutorily required books and records, but also failed to provide source documentation to substantiate its above assertion. Thus, given the totality of the circumstances, in the absence of other supporting documentation, the Department is not able to agree that Taxpayer met his burden of proof to demonstrate that the proposed assessment is wrong.

FINDING

Taxpayer's protest is respectfully denied.

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